

LETTER 944

July 30, 1986

July 18 DJIA 1777.98; PTI 2321; A-D Ratio -7.09
July 25 DJIA 1810.04; PTI 2334; A-D Ratio -6.87

THE PICTURE: You should probably read the "Super Boom" section of this Letter first, because in it I deal with the major or long-term picture. But for the intermediate-term, I must say that I've seldom seen a more fascinating market situation.

Let's begin with some classic Dow Theory. But first I will say again that I can't for the life of me understand why almost NO ONE is looking at this market from a Dow Theory standpoint. After all, the Dow Theory has outlasted every other technical method ever devised. The Theory, in fact, has provided the basis for almost all other technical methods, and I personally feel that Dow's Theory, over the years, has proved to be more accurate and more helpful than any other market method.

I've been talking in Letter after Letter about that April 7 Dow low of 1735.51. Please study the page 1 chart below. Note that the LAST CONFIRMED HIGHS (i.e., the last highs recorded by BOTH the Industrials and Transports) were established in late-March with peaks of 1821.72 for Industrials and 830.84 for Transports. Following those highs, the two Averages declined with Industrials dropping to a low of 1735.51 on April 7.

After the 1735.51 low both Averages rallied, and it was here that the long series of non-confirmations appeared. To be more explicit, note that after April 7 the Dow pushed to record high after record high -- but each time the Transports failed to confirm (in fact the Transports carved out a series of lower peaks and lower lows, a situation that every analyst in the nation pointed to with alarm).

But ironically, Wall Streeters (both amateur and professional) were concentrating on the WRONG THING. The really important factor was this: despite persistent and dramatic Transport weakness, the INDUSTRIALS WERE NOT CONFIRMING ON THE DOWNSIDE. Thus, from a Dow Theory standpoint, we were watching a bull market that was producing a series of new record Dow highs -- while the weakness in the Transportation sector was being ignored (i.e., was NOT being confirmed). This was, and still is, a bullish situation under Dow Theory, even though 95% of the Wall Street experts DID NOT UNDERSTAND (and apparently still don't) what the Averages were saying.

The worst of the Transport weakness (as of this writing) appeared on July 21, at which time the Transportation Average closed at 720.38. On the same day the Dow closed at 1779.11, still a fat 44 POINTS ABOVE its April 7 low. The Industrials never got close to confirming this new low of the Transports. So from the standpoint of Dow's Theory we are continuing to see that April 7 Dow low of 1735.51 HOLD despite Transport weakness, despite rotten business news, despite less-than-inspiring corporate reports, despite rising pessimism, and despite dire predictions from various well-known Wall Street "experts."

CONCLUSION: As long as 1735.51 on the Dow holds, I consider the SECONDARY trend of this market to be bullish. There has never been any question in my mind about the bullishness of the PRIMARY trend of this market.

Comments: The best kind of market you'll ever see is one that HOLDS IN THE FACE OF BAD NEWS. So far, that's what we've been seeing ever since April 7. Of course, this can change,

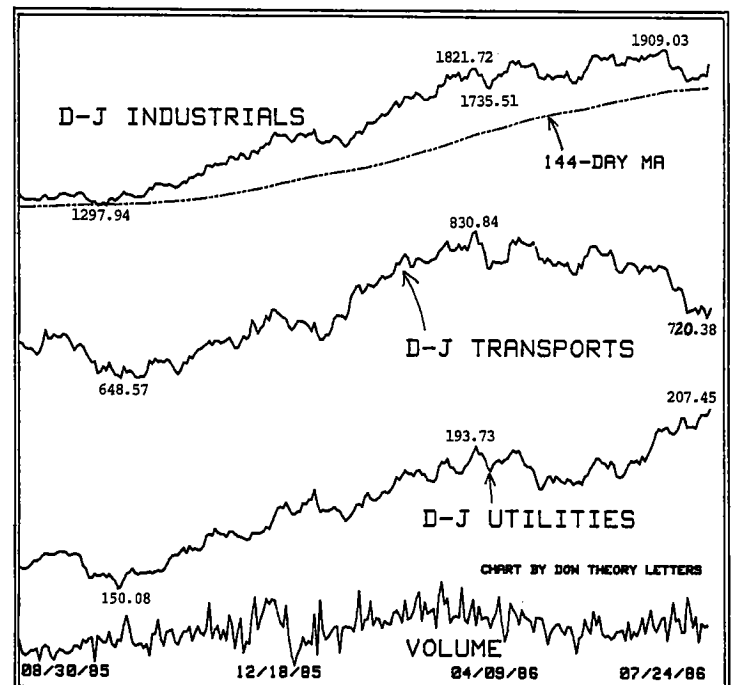
the Dow can break down, but the Dow has now had three months to confirm on the downside and it hasn't done so yet! Consequently, I rate the market's performance as BULLISH.

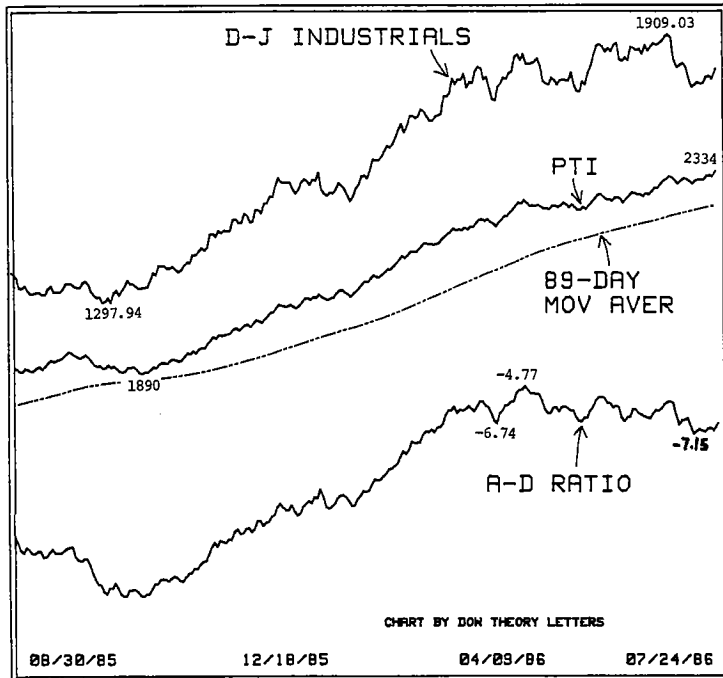
Next, I love a market that holds while the shorts build up. The shorts (even allowing for the arbitrage shorts) are pessimists that are betting on the downside as strongly as possible -- with their hard-earned greenbacks! Now consider this: the NYSE announced that for the period ending July 15 the short position on the NYSE jumped 18 million (5%) to a record high of 367 million. On top of that, it was announced that the short position on the AMEX soared 28%. What does this mean? To me all it means is that the bears are using up their ammunition as they try to knock a CONFIRMED BULL MARKET down. Good luck bears.

On July 23 my Primary Trend Index rose to 2331, a new record high. The PTI is based on eight "action-of-the-market" averages and indices. When it goes to new highs, it is telling me that the technical structure of the market is growing stronger. The new high in the PTI represents strong bullish technical pressure under Wall Street.

My 144-day exponential moving average of the Dow is now (1750). Note on the page 1 chart how the Dow has been holding persistently above the moving average, even as the moving average itself has been climbing into all-time high territory. This is one of the simplest of all primary bull market relationships. It's a relationship which, for some reason, most analysts have been ignoring. Personally I give a great deal of credence to this relationship. It's the fundamental sign of the bull.

The Utility Average on July 23 hit another all-time record high. The utility stocks are sensitive to (1) the action of the regulatory





authorities, (2) broad use of energy, (3) the direction of interest rates, (4) general business conditions. Because of this, a Utility Average that is setting record highs is a very positive indication for the general market.

Second conclusion: The LONGER the Dow holds above the 1735.51 level, the greater the build-up of the BULL MARKET PRESSURES. Furthermore, with the Dow refusing to confirm the Transports on the downside and with the Utility Average at record highs along with record highs in my PTI, I must identify this as another buy spot in the bull market.

As older subscribers know, I have labeled this whole affair a BUY 'EM AND HOLD 'EM TYPE OF BULL MARKET. We don't trade the dips and pops, we don't indulge in "in-and-out" trading, we don't try to outguess the primary trend, we do continue our policy of ACCUMULATING good dividend-paying stocks (along with high-grade bonds) as this bull market goes along. In primary bull markets, the great fortunes are made by those who buy and hold and then have faith that the great primary forces of the bull market will work in their favor. So far, that's been the story, and I believe it will continue to be the story.

SO MY ADVICE IS: BUY GOOD STOCKS AND HOLD THOSE STOCKS. THE STOCK MARKET REMAINS IN THE GRASP OF THE BULL. The more pessimism you now hear, the more bear arguments you hear, the more shorting and trading advice you now hear, the better. The bears simply do not understand how markets work or how they discount the future. In time they will either learn or be wiped out! I've seen it happen dozens of times before.

INVESTMENT POSITION: All right, here I go again, getting ready to make the most basic of all statements about investing. Ready? THIS IS STILL A PRIMARY BULL MARKET. For illustrative purposes (or for those who only believe what they can see), the bull is in the box.



I hardly think I was responsible for the current utility stock explosion, but I have been particularly bullish about the utilities ever since 1983. Furthermore, I've been recommending utilities (electric and water) for a couple of years. Is it possible that you still have not purchased any utility stocks? It's not too late, even though the utilities have been careening upwards. The water utilities get much less publicity than the the electric, and I like Amer. Water Works (AWK), Consumers Water (CONW), South. Calif. Water (SWTR). For electrics I like Florida Progress, Central Southwest, Delmarva Pow. & Lt., Kansas Pow. & Lt., Potomac Electric, South. Cal. Edison.

For long-term buy and hold stocks I like Amer. Express, Bristol Myers, Coca-Cola, Amer. Home Products, Philip Morris, Woolworth (even after the extraordinary rise, its P/E ratio is only 8.3). Let the market rest here if it wants. Personally, I'd like to see the major averages sit tight for the rest of 1986.

BACK FROM Well, I'm back from quintuple bypass (open-heart) surgery. Here are a few paragraphs about how it works. You start with a totally dedicated team of three (3) cardiac surgeons, all of whom have put in half their lives towards learning the techniques of heart surgery -- from medical school (four years), internship (couple of years), residency in general surgery (two years), then a special residency in cardiac surgery (two years). After all that study and hard work, these dedicated and obsessed characters are about 35 years of age and ready to start making a real living. Their living usually involves 12- to 14-hour days and (finally) an annual paycheck of up to a million bucks a year or more. These surgical teams (usually three cardiac surgeons) can perform one to even four operations a day, and they'll work five days a week with an emergency often thrown in on the weekend.

So here comes Richard Russell, the know-nothing patient. I walk into the head surgeon's office, and I note that he has a degree from Columbia as well as a degree from Stanford. Well, my father went to Columbia, and my wife, Faye, went to Stanford, so right off the bat I get good vibrations. On top of that, this surgeon (who operates day after day) is totally enthusiastic about surgery. He pulls out a one-foot heart model, discusses exactly what he intends to do and why, and as for me, I'm not even taking all this fascinating heart discussion in (although Faye is). I'm too busy studying this guy and picking up the vibrations and trying to decide whether I want to trust my life to him. Thirty minutes go by, and I'm sold.

Two weeks later I go to the hospital for preparation; a day later it's into surgery. Six hours of surgery go by, quintuple bypass, three guys with their hands in my chest, plus a fourth doctor (the anesthesiologist) standing by, and it's done. I wake up, and I say, "I can't believe it, I've lived through it, I'M STILL ALIVE. GLORY TO GOD!" The following day the pain begins. As I become fully conscious the pain gets worse. It feels like somebody's put an eggbeater in my chest and given it about ten good turns. On top of an eight-inch scar on my chest, there's a twenty-inch scar on my right leg where they've removed a vein for purposes of the bypass.

As the full brunt of the pain hits, I say to myself, "What's so good about being alive? You know, I think I made the wrong choice. Nothing is worse than this! Nobody told me it would be like this." But then I remember my family and I remember that I got through World War II and I got through a heart attack and I survived a fierce motorcycle crash and I got through a mastoidectomy and on and on. So I rethink my situation and the pain and I conclude, "Yeah, I got this far and being alive is definitely better than being dead." Ah, the great triumphs of the human soul!

Three days later the pain is subsiding to some extent. I'm walking ("staggering") around the room, and I'm asking about my kids. On the fourth day I ask Faye where the Dow is, and what the Transports are doing. At that point Faye knows beyond a shadow of a doubt that the worst is over and that Richard Russell is in his

own new bull market. On Tuesday, seven days after the bypass, I'm home sitting behind the Macintosh and writing this piece. "You're crazy," shouts Faye. "You're supposed to be resting." "In a minute," I reply. "But right now I'm having too much fun."

At this point I want to thank the literally hundreds of subscribers who sent get-well cards, flowers, fruit, books, cartoons, letters of encouragement. At first I intended to answer each and every item, but I can't do it. One of the things that happens after bypass is that you are extremely anemic, and that leaves you with very little energy. I figure that the best thing I can do for my subscribers at this point is put my energy into these reports, and that alone isn't easy.

But again, thanks to all you people for being so kind. I read and enjoyed every letter, book, and note. And I feel like Mr. Fruit and Flower of 1986. Thanks!

SUPER BOOM? Everyone seems confused as to what's happening in both the markets and the economy. The discount rate is now down to 6% while the bank prime rate has been cut to 8%, its lowest level in eight years. The producer (wholesale) price fell to 6 1/2% during the first half of 1986, its biggest decline since 1949. Crude oil is fluctuating at \$10-12 per barrel level, while the CRB Commodities Futures Index (27 commodities) recently dropped to 196, its lowest level in seven years.

Everywhere you look corporations are cutting their work forces, as they continue their concerted effort to get "lean and mean." On the farms (those that are left), agricultural prices are pathetic and surpluses of grains are so huge (due to loss of US export markets) it is rumored wheat and corn are piling up in the streets.

In the meantime, wonder of wonders, the stock market, historically the best barometer of business, is not acting half badly. What's happening? Has Wall Street lost its collective mind? Have the brains of Wall Street been par-boiled by the record hot weather of summer 1986? Time will tell, but let me remind you that the stock market is a BAROMETER, not a thermometer. What's the difference in the two? A thermometer tells you where you are now, while a barometer gives you hints and suggestions regarding what lies AHEAD.

Let me put a series of premises to you. Let's say that the market has NOT taken leave of its senses. Let's say that the stock market indeed possesses the rare ability to look ahead -- maybe six months to even a year ahead. Let's say that US business is going to get rough (of course, it already is), but let's say that it's going to get even rougher. Then let's say that the stock market knows all about how rough things are today and how difficult they're going to be this summer and into the fall and maybe even into the winter. Finally, let's suppose that all that bad news is already BUILT INTO the stock market. If we concede all that, then isn't it possible that the market is telling you and me and the politicians and the newspaper reporters and the financial editors something that they are too blind or too egotistical or too short-sighted to see? I've seen this same set of circumstances before, most dramatically in late-1957 and again in late-1974.

In my opinion, the stock market could be looking ahead to the time when the easy money policy of the Fed and the comparatively low interest rates and the "cheap dollar" and the new tax bill all start having a bullish effect on business. It's happened dozens of times before that the stock market has held fast or actually moved up in the face of poor and even worsening business. So, what's so amazing about today's performance? And why are all these "expert analysts" so convinced that the stock market must perform in accordance with their dire economic prophecies? What makes these characters smarter and more perspicacious than the stock market barometer? That's the question we might ask ourselves as we pick up (with trembling hands) the latest issue of our local newspaper.

Now let's take all the foregoing one step further. I want to enlarge on this thesis in the following section. In reading piles of economic reports and opinions, it occurs to me that one scenario is strikingly absent. It's the scenario of a coming "super-boom." I read about deflation, sagging business, foreign competition, depression areas in agriculture and in the oil, but it's interesting that I read nothing about the chances of a major economic boom waiting to happen, say in 1987 or '88.

Ordinarily, I wouldn't think in terms of a super-boom — except for the fact that almost no one else is. Yet, consider this: the stock market at present seems to be marching to the rhythm of a different drum. With all the troubles we read about, why is the Dow still within striking distance of its all-time high, why is my PTI at a record high, why is the market breadth (A-D ratio) moving sideways instead of collapsing, why indeed did the A-D break out above its nine-year trading range back in 1983 (see Letter 939, page 3)? And why is the Utility Average hitting successive new all-time highs (and this is a particularly important question, since the Utility Average has, in recent history, tended to be a market bellwether)?

When the market acts contrary to the obvious, it always sets me to thinking the non-obvious, the unexpected. What would be the least expected economic scenario to occur during the years ahead? It seems to me that one could make a good contrary opinion case for a coming super-boom.

How could a super-boom happen? Let me list a few of the items that could lay the groundwork for a super-boom. First, the historic drop in energy prices. The drop lowers business costs across a broad spectrum. Next, the historic decline in interest rates. Here again we have a huge drop in the cost of doing business. Next, the disinflationary or deflationary trend which began in 1980 but which is only now becoming obvious to the average American. The perception of deflation could bring a move to savings. When a person sees the buying power of his dollars rising, he is far more tempted to save (since in deflation, dollars are worth more through time rather than less).

Nothing is in the bag, but it seems almost certain that we will have a new tax code in the US to take effect sometime during 1987. The general opinion is that the new tax code will be good for the nation — although there may be a painful period of adjustment first. But some of the adjusting may be taking place now, as certain elements of the code become known. Certainly one item we can count on is the end of most tax shelters. A second item is that most people will take home more money under the new code. Maybe not a lot more — but MORE. And to the average American, that's bullish.

Now listen to these words from my friend Arthur Gray Jr., president of Dreyfus Personal Management, Inc. (from a letter written July 15):

"What will tax reform mean to you? For the first time in half a century a dollar earned will be as valuable as a dollar saved through tax shelters. The current 46% corporate rate plus a 50% top personal rate results in the Federal Government taking 73 cents of every invested dollar of profit. What a drag on our economy. With a 33% corporate rate and a 27% individual ceiling approximately 50 cents of every dollar of profit will accrue to shareholders. Hold on to your hats.

"What about the increased tax on Capital Gains? Although long-term capital gains rise from 20% to 27% (a 35% increase) short-term capital gains are lowered from 50% to 27% (a 45% decrease). No longer will there be any holding period for taking profits. The stage is being set for 300 million share days on the New York Stock Exchange. For the first time in its history, the Dow Jones Divisor has become a multiplier, which means that if each of the 30 Dow stocks advances (or declines) one point, the average moves 33 points versus 3 points in 1929 and 13 points 20 years ago. Before the great bull market of the eighties is over, be prepared to see daily swings of 50 to 100 points on the Dow.

"The new Tax Reform Bill will encourage corporations once again to write off everything possible in the last quarter of the year so that reported earnings may not exceed \$130 for 1986. Looking ahead to 1987 Dow earnings should reach \$160 -- and our real GNP growth forecast of 5% plus with still another year of inflation below 5%, we believe, justifies a 15 x P/E multiple, bringing the Dow to 2400 by December 1987."

Perhaps the most important consideration of all: This nation and its leaders are beginning to chaff under the unfair export rules that American business has been forced to live under. Foreign nation after foreign nation has set up UNFAIR BARRIERS to US goods, thereby forcing American manufacturers into a corner and preventing them from selling their own merchandise. My own feeling is that Pres. Reagan and the Congress have "had it" with these foreign restrictions -- and I think we are close (finally) to getting tough with those nations who have literally prohibited the import of US goods. If these unfair rules are changed, I think this would be a huge plus for American business. And the horrendous US balance-of-payments deficits tell me that it is not going to be long before the US starts fighting the outrageous restrictions that its businessmen must submit to. In other words, I believe it is just a matter of time before the US calls a halt to the policies (on the part of our "trading partners") that have produced these intolerable balance-of-payment deficits.

Then there is still another consideration that could underly a coming boom. I have written about this before, but I will repeat it. The massive rise in the value of both stocks and bonds since 1982 has added tens of billions of dollars in net worth to individuals, corporations, and institutions. This immense increase in wealth will, in due time, filter into the system and will work toward optimism on the part of Americans. To cite a single example of what I am talking about, the Wilshire 5000 Equity Index is a good proxy for the stock markets. During the last 12 months alone, the Wilshire has increased in value by half a trillion dollars. This is half the size of the US federal debt. And the value increase in the bond market (the bond market dwarfs the stock market) has been substantially larger. Thus, wealth in the US, in terms of securities, has increased tremendously.

So what I'm saying is that there is a fascinating contrary opinion out there, and it is not out of step with the stock market (and remember, the stock market has been our most reliable barometer of coming economic events). The contrary opinion is that conditions are slowly ripening for a US super-boom. I know, given the current state of business, this thought seems almost absurd. But I'm not eliminating the whole concept of a super-boom from my own business thinking and investment planning.

Q & A: Question: I know you are not sold on cycle studies. What about the astrological market studies that I often read about?

Answer: In this business you learn not to laugh at anything. I know that there are some very intelligent people who put a lot of credence in astrology, and, more particularly, astrology pertaining to the market. I guess I'm not one of them, but I usually read such reports with interest. One of the more serious and successful reports is turned out jointly by Jim Fraser and Harriet Higginson (PO Box 772, Setauket, NY 11733). The funny thing is that these people have been very right on the market and the economy for quite some time. They are, in fact, carrying on the work of the Hasbrouks, whose work I followed for years.

The Fraser-Higginson "Space-Time Forecasting" report believes there is an overriding 36-year cycle that is in force. This cycle produced major highs in 1893, 1929, and 1966. They believe another such watershed high will arrive in 1991 (this cycle is supposed to be based on the positions of Saturn and Neptune which are responsible for the 36-year cycle). The forecast of the 1991 high particularly interests me because of my own thesis that

this bull market could fool the great majority by being subject to many difficulties in the years ahead, and therefore being EXTENDED in both its duration and in its ultimate height (for instance, is there anyone who believes this bull market could last another five years?).

Question: Russell, you've discussed and recommended the closed-end funds (listed on the NYSE) often in the past. What's been happening to those funds?

Answer: Most of them have been doing well in this bull market. I continue to like them -- especially at this time. The closed-end funds are managed funds which are closed in that when you buy into one you are simply buying the fund from another investor in the same way that you buy GM or Woolworth. This differs from a mutual fund in that when you buy into a mutual fund (which is an open-ended fund), you are buying shares that are issued to you by the fund. Each time you buy a mutual fund the total assets of that fund rise by the amount of your purchase. But when you buy a closed-end fund your purchase does not affect that fund's assets. It's just a trade with another stockholder.

Closed-end funds sell at whatever the market dictates, so that at times they may sell above net assets, and at other times they may sell at a discount. Right now, interestingly, almost all the closed-end stock funds are selling at discounts. For instance, Tri-Continental (the largest of the closed-end funds with assets of over \$1.3 billion) is selling around 30. But it has net assets of \$34 a share and is selling at a discount to assets of almost 12%. Lehman Corp. is selling at a discount of 11.5%. Adams Express is selling at a 12.8% discount. Niagara Shares is at a 13.1% discount.

These closed-end funds are attractive now because they present a double-barreled way of investing in the market. In a bull market they will obviously follow the market up, but they often do so in a sporadic fashion (as opposed to a no-load fund) which always sells at exact net asset value). But when a bull market finally gets smoking on the upside, the closed-end funds can sell at very close to net asset value or even at a premium.

I often use the discount or premium differential on the closed-end funds as a barometer of the public's enthusiasm for the market. Right now, for instance, I feel that the closed-end fund profile presents a bullish background for Wall Street. I say this because the funds are almost all selling at good discounts. When the public finally gets hot for this market I would expect the no-load funds to sell at very close to net assets or even at premiums rather than discounts. (By the way, each week Barron's carries the whole list of closed-end funds along with their assets under the column labeled "Publicly Traded Funds.")

NOTES & QUOTES: The world of stocks is becoming just that — one world with investors now buying stocks on many exchanges. But the three leading exchanges in the free world are (1) The New York Stock Exchange with its international legal tender, the dollar. The NYSE is the biggest, holding half the world's \$3.5 trillion in equity capital. (2) Tokyo is now the second largest exchange, and this is the up-and-coming "hot" one. The yen is becoming an international currency and Japan is liberalizing its exchange rules (there are now nine seats on the Japanese exchange owned by foreigners, one by Merrill Lynch). (3) The third biggest exchange is London. The British exchange has the greatest geographical advantage, being in the same hemisphere as 13 of the 20 major international exchanges. On October 27 London will introduce an important deregulation package which will put London in a competitive position (on commissions) with both New York and Tokyo.

Increasingly, stocks are being cross-listed on the various exchanges. Thus you can buy GM in Switzerland or Honda on the NYSE or Sumitomo in London. Over the last few years with the various foreign exchanges outperforming the US markets, a number of foreign-oriented mutual funds have been formed, as well as numerous closed-end funds on the NYSE (Japan Fund,

Mexico Fund, Korea Fund, etc.) So what we have now are global markets with US investors now comparing stocks and markets on dozens of exchanges.

I wonder if this isn't going to ultimately give us one huge global BULL market with a final INTERNATIONAL speculative binge unlike anything we have ever seen? I wonder.

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The state of Florida is now booming, with a current population of over 12 million. Thus, Florida joins the sun-belt states of California and Texas as a "big population" state. Both Texas and Florida possess the attraction of no personal income taxes, while Florida and California possess the added attraction of a no-snow and generally warm climate. So huge and expanding is the population in these three states that it is estimated that by the year 2,000 the three states will account for 25% of all the members of the House of Representatives!

* *

I've been saying since 1980 that with the huge US debt (we've mortgaged the future), one thing is clear: The American standard of living is heading down. I further stated that our children will not enjoy the same high standard of living we have enjoyed (they'll be wrestling with OUR debts), and the proofs are now coming in. Ponder this fact: average weekly earnings (adjusted for inflation) which have been held down by a shorter work week, have declined an astonishing 14.3% since 1973. The median household income (\$26,433 in 1984), has dropped 6% (again adjusted for inflation) since 1974. Lest you are confused, these facts do not mean or imply that the US cannot have speculative market booms now or in the future; no, these facts apply strictly to the US standard of living.

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The investment advisory business must be getting tougher. I say this on the basis of advertisements I see in Barron's, Investor's Daily, Financial World, Forbes and in the newspapers. Many of the ads are becoming absolutely shrill, promising pinpoint timing, offering testaments to their own past brilliance, and boasting of new exciting methods for picking the one stock in a hundred that is almost guaranteed to double or triple over the next year.

It's sad but true: when you see these kinds of ads it doesn't mean that analysts are getting smarter or even luckier. No, it means that competition is getting fiercer, and the advisors therefore feel that they have to promise more in order to try to get subscriptions.

It's not only dangerous to promise too much in this business, it's deceitful. Old pros know that if you guess or predict, and your predictions are 60% correct, you're doing better than most. The fact is that those who have been in the business the longest and those who have been through three or four complete bull and bear cycles are the most reluctant to make blatant and boastful promises.

In the advisory business, I personally like a writer who (1) has a sense of history, (2) exhibits a feel or an intuition for the market, (3) possesses a healthy skepticism, (4) understands the meaning of money and the concept of compounding, and (5) has the guts to admit it when he is wrong, which is another way of saying that he has at least a modest portion of humility.

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Despite the damning evidence, one-third of all American adults still smoke. In China it's worse. A recent survey found that 70% of Chinese men smoke -- and the percentage is rising.

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Speed: After 25 years of motorcycle riding, I finally quit (two years ago). In those 25 years I only had one bad accident (going down at 65mph with a broken bearing and a resultant high-speed wobble -- and boy, did I lose skin). But I still watch the cycle news along with the various specs and statistics. In recent years motorcycles have gone high-tech, probably more so than autos. Now here's a

statistic for you. Ferraris are known as fast cars, and the Ferrari 308 GTS goes from 0 to 60 MPH in 7.17 seconds, according to Motor Trend Magazine. But the new Suzuki GSXR-750 motorcycle goes from 0 to 60 in 2.8 seconds, according to tests from the Feb. '86 Cycle Magazine. Of course, I don't know where you can use this kind of speed, but it makes for good macho reading.

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From our "Keep Trying" Dept: Twenty-five years ago Chester Carlson invented a copy machine. He tried in vain to sell it. Between 1939 and 1944, 20 different corporations turned down his invention. Finally, a little outfit called Haloid took on Carlson's invention. Haloid spent 10 years and \$12 million perfecting the copier. Then Haloid changed its name to Xerox, and a new industry was born. Now machines of various kinds turn out roughly 500 billion copies a year. Twenty-five companies make copiers, and industry sales are \$27 billion a year!

* *

Medical: A new product (concentrated fish oil in capsules by Scherer) has received favorable mention from 13 medical journals this year. Fish oil, it seems, can help prevent hardening of the arteries, one of America's most prevalent diseases. The "MaxEPA" capsules are sold as a food supplement, NOT a drug, and sales are BOOMING. ... The medical community is worried about over-load: In the last two decades there has been an 84% increase in the number of doctors and a 50% increase in the ratio of doctors to population. ... Specialization is in. Amazing fact: Heart bypass surgery is now one of the commonest major operations in the US with over 250,000 operations each year. In NYC 12 doctors perform 99% of all heart surgery today! Each earns over \$1 million per year (and I'm sure they deserve it). ... College women are twice as likely to smoke as college men. But here is an unbelievable and damning statistic: women tend to have fewer heart attacks than men. But in women who do have heart attacks, 85% (that's eighty-five percent) are smokers! In other words, if a woman today has a heart attack, you can almost bank on it -- she's a smoker!

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From an interview with James Mills, author of the new book, "The Underground Empire" published by Doubleday. The annual international sales of narcotics now exceeds half a trillion dollars. That's more than three times the value of all the US currency in circulation. It's more than the gross national product of all but six of the major industrialized nations. By the way, I'm now reading this book and it's a mind-blower. I recommend it as far more interesting, exciting, and informative than any fiction you can find.

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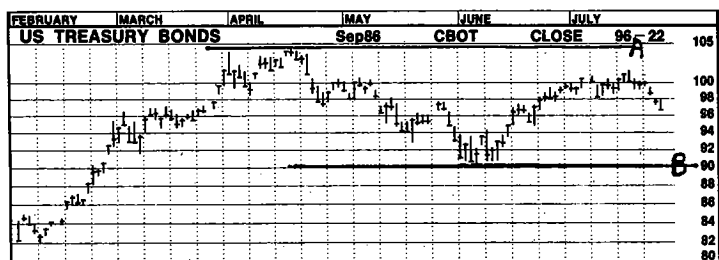
For decades wine producers in the US have tried to get Americans into the wine drinking habit. But except for the East, Americans are still basically beer and whiskey drinkers. Ponder this: The average amount of wine consumed by an individual in France is 25 gallons per year. Average amount consumed by an American ... 1 gallon.

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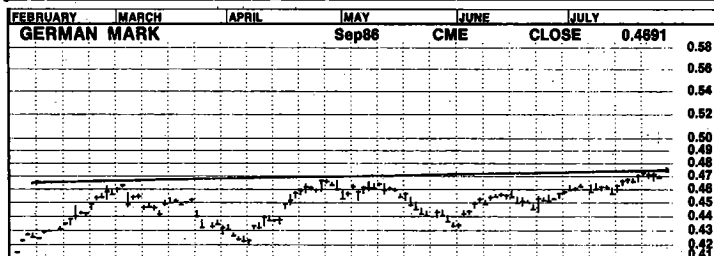
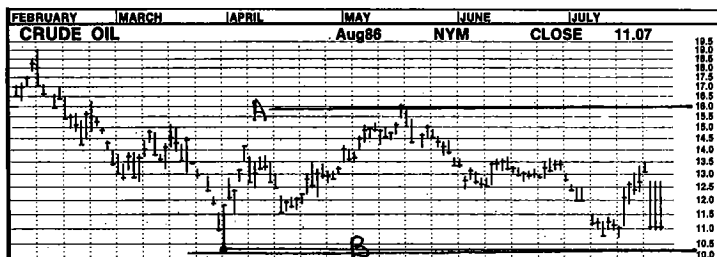
Taxes: How will you do with the new tax bill on a state income tax basis? First, the states with no personal income taxes will not be affected. These blessed states are Alaska, Connecticut, Florida, Nevada, New Hampshire, Tennessee, Texas, Washington, Wyoming. States where state tax increases are almost a sure thing (due to revenue shortfalls) are Illinois, Kansas, Michigan, Minnesota, Missouri, New York (maybe a \$2 billion increase), Ohio, Virginia. Tax decreases can be expected in Nebraska, North Dakota.

CHARTS: The daily chart of the T-bonds (Sept. futures) shows what I've been suggesting all along -- a trading range (A to B on the chart) with a clear top in April and a bottom in June. Meanwhile, Wall Street traders have been driving themselves nuts trying to figure exactly what the near-term trend is. Forget it guys, you can't make the market do something it isn't ready to do. I

continue to hold all my own muni bonds. I still think the underlying (primary) trend of bonds is bullish.



The crude oil chart shows me the same broad A to B trading range. There seems to be real support for the August contract around 10. I could be very wrong, but I'd be surprised if 10 is broken.



Here's the German mark in terms of dollars (Sept. Futures contract). And this area (the mark and the yen) represents one of the BIG US problems. The US would like the Germans to inflate a bit and thereby help the US economy -- German imports would then increase. But the Germans, so far, are saying "nein." The US is also suggesting that Japan lower its interest rates and thereby "give us a break." Japan is shaking its head, "No."

Personally, I think Washington is losing patience, and with 31 US states now in recession (the worst being Texas, Louisiana, and Oklahoma) we're nearing the "no more mister nice guy" stage. Politics is now entering the picture in a big way. With intimations of "a full recession" maybe on the way, the Republicans face the frightening specter of losing control of the Senate. Now if there's anything calculated to make a politician move his fanny, it's the idea of (1) losing control of one of the houses, and (2) losing his job.

LATE NOTES: I don't know how many of my readers fully grasped the rather complex Dow Theory discussion on page 1. But let me emphasize one item: a primary bull market that won't go down in the face of adverse economic news is a primary bull market that wants to go higher (or at worst, wants to establish a high-level trading range). After recording an April 7 low of 1735.51, the Dow rallied to new highs and then **PERSISTENTLY REFUSED TO BREAK THAT 1735.51 LOW**. That's what I've been shouting about ever since mid-April. We've got a bull market in which (1) Industrials won't confirm on the downside, and in which (2) the bellwether Utility Average continues to set record highs — all this against a background of poor economic news and a steadily rising short interest. That is powerful primary bull market action, and anyone who tells you differently doesn't know how to read markets!

My own inclination here is to continue to buy the strong growth stocks, the big name growth stocks like MMM, Coke, Amer. Home Products, Bristol Meyers, Amer. Express, Exxon, DuPont, JP Morgan. I know that your broker is probably telling you to pick up

those little known marvels on the OTC market, but I like the big growth stocks, and I think they're going to look awfully good before this bull market breathes its last. And as you know, I continue to like the utilities.

Late, late notes: The encouraging letters and get-well presents keep coming in, and I can't thank my readers enough. Crazy Marty Zweig sent me a huge batch of silver balloons that about fill our entire kitchen -- from the ceiling down. I'm off oxygen now, and thanks to you, Marty, I'm breathing pure helium.....I just received the latest Harry Schultz report, and Harry senses coming "deflation, depression, credit crash, bank closures, runaway AIDS, earthquakes" and you name it. In an open letter to me, my old buddy implores me to pack up and join him in Monte Carlo before it's too late. In my next report, I'm going to publish Harry's letter to me -- together with my dramatic answer. Don't miss it!

GOLD: Would you like to go nuts? Want to pull your hair out? All right, then read the well-reasoned, even brilliant interview with Al Friedberg in the latest (July 28) issue of Barron's. In this article Friedberg (head of a Toronto-based broker group) states that (1) the dollar is still in a bear market and could go much lower, (2) oil should go to \$5 a barrel, (3) US stocks and bonds are too high and will be heading down, and (4) gold is a bargain at today's prices as are commodities, and both will soon be heading higher. Friedberg notes (as have I) that although commodities have been in a big bear market, gold since February 1985 has been slowly rising. This peculiar phenomenon, thinks Friedberg, is a reflection of the thesis that gold is now very cheap in the eyes of international investors. He thinks Japanese, Swiss, and German investors are beginning to see gold as a bargain, and that they will soon be dumping US stocks and bonds (which Friedberg thinks are too high) in favor of today's bargain-basement item — gold.

Boy, it's a good argument. As you well know, I've been watching gold crawl up from its 285 low of February 1985, and I've noted over and over that it was doing this in the face of a continuing commodity collapse. Someone, I said, was accumulating gold even while wheat and corn and cotton and copper were going into the tank. Pretty strange action! So could Friedberg be right? Are we on the edge of inflation again, and is gold about to lead the way? My answer: sure Friedberg could be right, but I want to see his ideas backed up by **MY MARKET STUDIES**. If I had acted on the words of every confirmed genius who appeared in the pages of Barron's or Fortune or Forbes I'd have gone flat broke years ago. I listen to the words, sure but it's the markets that make my music!

One of the items that I've followed for years is my simple ratio of gold divided by common stocks (I use the NYSE Composite as a proxy for stocks). When the ratio is in a rising trend I know that the world is protecting itself against inflation and opting for gold as opposed to stocks. When the ratio is in a declining trend I know the world is opting for financials and that the smart boys are buying stocks (and usually bonds) as opposed to precious metals.

So what's actually been happening? On January 3, 1980 my gold/stock ratio stood at a lofty 1050. From there it started down, even as gold crashed. On January 3, 1984 the ratio was down to 405. January 3, 1985 saw the ratio at 320. January 2, 1986 and the ratio was 270. The low on my tabulations was reached on July 2, 1986 at 235. That's been **THE LOW** so far, and if Friedberg's theses are correct, my ratio shouldn't go much lower. In fact, it should turn up and break above its long-term declining trendline. Friedberg is smart, but smart guys can be so wrong you wouldn't believe it. So what I'm saying is that over the years I've learned to respect the smart guys (including even myself), but I **ACT ON WHAT THE MARKET TELLS ME**.

So I'll be watching my ratio (as I always do) and if it turns up decisively in favor of gold, my subscribers will be the first to know about it. And we'll take appropriate action. Until then, if you're a goldbug you'll love the Barron's article. But if you're a market man, just keep buying a few gold coins each month (as I've advised all along). But don't be a big gold bull. No, not until the technical evidence comes in, and it is not here yet.

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